

PS [redacted] District
P [redacted]

5-7-33

5/7/93

FEB 19 1993

Employer Identification Number: [redacted]
Key District Office: [redacted]

Dear Applicant:

We have completed our consideration of your application for recognition of exemption from federal income tax. We have concluded that you are not exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code. The reasons for our conclusions are explained below.

The information submitted indicates that you were organized as a nonprofit corporation under the laws of the State of [redacted] on [redacted].

Your purpose, as stated in your application for exemption, is to arrange for the provision of medical services through your members to enrollees of managed care plans. Each of your members must be a licensed primary or specialty care physician in good standing with the medical staff at [redacted].

You have entered into an agreement with Hospital to create a corporation to be known as [redacted] (Company) which will develop joint service arrangements with various purchasers of clinical and related services operating in the managed care marketplace. Your organization and Hospital will be the sole shareholders of Company.

You have also entered into a provider agreement with Company to provide or arrange for the providing of services to the members of [redacted]. [redacted] includes Health Maintenance Organizations, Preferred Provider Organizations, Preferred Provider Arrangements, and such other forms of arrangements which enter into a contract with Company under which Company agrees to arrange for the provision of all medically necessary health services to member-patients.

Under the provider agreement with the Company, the Company or [redacted] will transmit payments to you for authorized covered services to member-patients in accordance with Company rules, less the

Company administrative fee. You will process and pay or arrange for the payment of all service claims for physician and related services provided to member-patients in accordance with Company rules.

You derive your financial support primarily from physician dues. In return for the payment of dues, you state in your application for exemption that "members will receive more efficient and higher compensation from managed health care organizations." The initial fee paid by participating physicians is nonrecurring.

Your Bylaws provide that at least sixty percent of the directors on your Board of Directors will be physicians who have signed a Participating Primary Care Physician Agreement with you.

Section 501(c)(3) of the Code provides for the exemption from Federal income tax of organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(b)(4) of the regulations provides, in part, that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will be considered dedicated to an exempt purpose, for example, if, upon dissolution, such assets would, by reason of a provision in the organization's articles or by operation of law, be distributed for one or more exempt purposes, or to the Federal government, or to a State or local government, for a public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgment of the court will best accomplish the general purposes for which the dissolved organization was organized.

Section 1.501(c)(3)-1(c)(1) of the regulations provides, in part, that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such purposes described in section 501(c)(3) of the Code, but will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.


Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more section 501(c)(3) purposes unless it serves a public rather than a private interest. An organization must, therefore, show that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or the creator's family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests. Moreover, the presence of a single nonexempt purpose substantial in nature, such as the promotion of the business activities of its organizers, will prevent exemption. See Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945).

Rev. Rul. 86-98, 1986-2 C.B. 75, provides that an individual practice association (IPA) that served as a bargaining agent for its members and performed administrative claims services could not qualify for exemption under section 501(c)(4). The Service found that the IPA operated for the private benefit of member-physicians since its primary functions were to provide its member-physicians access to a large group of patients.

Based on the information submitted, we have concluded that you are not organized and operated exclusively in furtherance of charitable purposes within the meaning of section 501(c)(3) of the Code. Your main functions are to provide an available pool of physicians that will abide by Company rules when rendering medical services to the member-patients of [REDACTED] and to provide your member-physicians with access to a large group of patients, [REDACTED] member-patients. You administer the claims for fees received from your member-physicians and pay them according to Company rules. Thus, you are similar to a commercial health insurance reimbursement program because you merely serve as an alternate method to the direct billing and collection of fees from patients.

Moreover, you are primarily operated for the private benefit of your member-physicians rather than the community as a whole since you benefit member-physicians by increasing the physician's market share and providing administrative services to your member-physicians. The physicians receiving the benefits control your organization. See section 1.501(c)(3)-1(d)(1)(ii) of the regulations and Rev. Rul. 86-98.

In addition, your corporate charter does not meet the organizational test of section 1.501(c)(3)-1(b) of the regulations because it does not include a provision that dedicates your assets to an exempt purpose as required by section 1.501(c)(3)-1(b)(4) of the regulations.


You are required to file federal income tax returns. Contributions to your organization are not deductible under section 170(c) of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement must be submitted within 30 days of the date of this letter and must be signed by one of your officers. You also have a right to a conference in this office after your statement is submitted. If you want a conference, you must request it when you file your protest statement. If you are to be represented by someone who is not one of your officers, he/she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements.

If you do not protest this proposed ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the United States Tax Court, the United States Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key District Director. Thereafter, any questions about your federal income tax status should be addressed to that office. The appropriate State officials will be notified of this action in accordance with section 6104(c) of the Code.

When sending additional letters with respect to this case to the Internal Revenue Service, you will expedite their receipts by placing the following symbols on the envelope: E:EO:R:1, Room 6516. These symbols do not refer to your case but rather to its location.

Sincerely,



Chief, Exempt Organizations
Rulings Branch 1

cc: 

cc: 